BILL # HB 2563 **TITLE:** cable television; services

SPONSOR: Gray **STATUS:** House Engrossed

REQUESTED BY: House **PREPARED BY:** Brian Cary

FISCAL ANALYSIS

Description

The bill would limit the franchise or license fee that a city, town or county could collect from a cable television system operator. For licenses extended or renewed after December 31, 2006, the license fee levied by a city or town could not exceed 1) its transaction privilege tax (TPT) rate plus one percent, or 2) 5% of the cable operator's gross revenue, whichever is less. For a county, the maximum fee would be the lesser of 1) the highest city or town TPT in the county plus 1%, or 2) 5% of the cable operator's gross revenue. The bill would also prevent a city, town or county from requiring a cable operator to provide either monetary or in-kind payments over and above the license fee. In-kind services would be limited to complimentary line extensions for cable service, complimentary cable service to governments and schools, and up to two public access channels.

Estimated Impact

JLBC Staff estimates that the bill would have no fiscal impact at the state level. The local impact would vary by political subdivision and would depend on several factors: 1) the difference between the current franchise fees collected and the TPT plus 1%; 2) the value of in-kind services that would no longer be received or would be paid for after new franchise agreement takes effect; and, 3) the dates when the existing franchise agreements are due to expire.

JLBC Staff cannot determine the local fiscal impact of the bill with certainty. In order to estimate the impact, we collected cable television franchise tax data for the eight largest cities in the state, which account for 58% of Arizona's total population: Phoenix, Tucson, Mesa, Glendale, Scottsdale, Chandler, Gilbert and Tempe.

The first of these cities to be affected would be Scottsdale, which would see its cable franchise fees decline by an estimated $(720,000) in FY 2008, $(750,000) in FY 2009, and $(777,000) in FY 2010. Tucson's cable tax collections would decline by $(940,000) in FY 2008, $(1.5) million in FY 2009, and $(1.5) million in FY 2010. Phoenix would lose $(5.0) million in cable revenue in FY 2010, while Tempe's FY 2010 revenue loss would be $(330,000). The remaining cities' franchise agreement expiration dates range from May 2010 to October 2018, so the bill's impact on them would occur further into the future.

Other potential costs include the value of current in-kind services that would require payment to the cable operator after passage of the bill. Public education and government (PEG) channels are the most significant of these potential expenses. At an estimated annual cost of $250,000 each, a city choosing to provide two PEG channels would incur an additional fiscal impact of approximately $500,000 per year.

The Department of Revenue did not estimate the bill's fiscal impact.

Analysis

In order to estimate the bill's impact, franchise fee revenue and tax rates were obtained for the eight cities mentioned above. To calculate the impact, cable revenue was assumed to increase by 3% per year for each city. The new maximum franchise tax rate specified by the bill was subtracted from the existing rate for each city, with the result multiplied by the cable operators' estimated annual gross revenue to calculate the net revenue change by city.

Phoenix's current franchise agreement with its primary cable franchisee does not expire until June 29, 2009. In FY 2004, the city collected $8.2 million in cable franchise fees. With the current 5.7% effective tax rate reduced to a maximum of 2.8% following passage of the bill, the city's cable franchise revenue would decline by $(5.0) million in FY 2010 and by an additional 3% annually in subsequent years. Should the city continue to provide PEG channels, they would cost an additional $250,000 each.

Tucson's primary franchise agreement will expire on October 30, 2007. It also charges cable operators an effective rate of 5.7% to operate in the city. Based on FY 2004 collections of $1.9 million, the lower tax rate required by the bill (3%) would yield changes in revenue of $(940,000) in FY 2008, $(1.5) million in FY 2009, and $(1.5) million in FY 2010, with the amount growing by 3% annually in future years. Costs for services currently provided in kind would depend on what the city would choose under any future agreement.

Mesa currently levies a cable franchise fee of 4.5% of gross revenue and collected $1.9 million in FY 2004. Its current franchise agreement does not expire until October 19, 2018. Based on a new tax rate of 2.5% and the assumptions described above, the city would lose $(860,000) million in revenue in FY 2019, plus the cost of any in-kind services.

Glendale has a current effective cable franchise tax rate of 5.7% and it collected $1.2 million in FY 2004. The new tax rate proscribed by the bill could not exceed 2.8%. Since its current primary franchise agreement does not expire until December 31, 2013, the bill's impact would not take effect until midway through FY 2014, when the city would lose $(410,000), followed by loss of $(850,000) in FY 2015. Payment for current in-kind services would produce an additional impact.

Chandler collected $1.5 million in cable franchise fees in FY 2004 and levied an effective tax rate of 5.7%, which would be limited to 2.5% by the bill. Its franchise agreement with its dominant provider will expire May 14, 2010. The estimated revenue loss from the bill in would be $(1.1) million in FY 2011. The city estimated that the cost of maintaining its PEG channels and the costs of other cable related services would effectively eliminate the estimated $800,000 in remaining revenue.

The bill's initial impact on Scottsdale would occur in FY 2008, when its cable franchise effective tax rate would be reduced from 5.7% to no more than 2.65%. The resulting revenue loss would be $(720,000), followed by decreases of $(750,000) and $(770,000) in FY 2009 and FY 2010, respectively. Additional costs may occur due to payment for services previously provided in kind.

Tempe would experience the bill's initial impact after its current franchise agreement expires November 17, 2009. Based on an existing tax rate of 5% and a new tax rate of 2.8%, the FY 2010 impact would be $(330,000), followed by $(580,000) in FY 2011 and $(600,000) in 2012. The cost of maintaining two PEG channels at $250,000 apiece would absorb most of the approximate $750,000 in annual revenue remaining in FY 2011 and FY 2012.

Gilbert's current franchise agreement will expire on January 25, 2014. With a current effective tax rate of 5.7% and a rate after the bill's passage of 2.5%, the initial FY 2014 revenue loss would be $(300,000), followed by $(740,000) in FY 2015. These amounts do not include any costs associated with future payments for current in-kind services.

The impact for smaller cities and counties would be roughly proportional to their population, would depend on their franchise agreement expiration dates, and would also depend on their current cable franchise fee structure. In some cities and towns, the current tax rate is actually below the maximum provided by the bill, so they would not experience a revenue loss. However, they may incur costs for cable services previously provided in kind. It is also possible that cities may increase their TPT rates in the future, which could reduce the potential revenue losses induced by the bill.

Local Government Impact

The JLBC Staff estimates that the bill would reduce revenues for local governments. See the discussion in the Estimated Impact and Analysis sections for more information.

3/18/05